

**THE SURETY & FIDELITY ASSOCIATION OF AMERICA**

**MEMORANDUM**

**TO:** Government Affairs Advisory Committee  
Contract Bonds Advisory Committee

**FROM:** Lenore S. Marema, Vice President-Government Affairs

**DATE:** June 26, 2007

**SUBJECT:** 2007 Overview of the State Legislative Sessions—Contract Surety

---

At this point in the state sessions, it is easier to list the states still in their regular 2007 session, as most states have adjourned for the year. California, the District of Columbia, Delaware, Illinois, Louisiana, Massachusetts, Michigan, North Carolina, New Hampshire, Ohio, Oregon, Pennsylvania and Wisconsin are still in session. New Jersey and New York are in recess, and South Carolina is in its veto session.

The following summarizes key state legislation affecting contract surety that SFAA has been working on most recently with AIA and the NASBP. This report updates the May 2007 overview report, which can be accessed on the SFAA website for reference.

**Bad Faith**

The trial lawyers resurrected their bad faith agenda in states that experienced a turnover in leadership as a result of the November 2006 elections.

**Rhode Island** SB 192 would have permitted any obligee, principal or claimant under a payment or performance bond to bring an action against the surety when it is alleged that the surety wrongfully and in bad faith refused to pay or settle a claim or refused to perform its obligations under the bond. Compensatory and punitive damages are permitted, as well as reasonable attorneys' fees. The bill passed the Senate but was heard and held again in the House Judiciary Committee. The House Committee previously heard and held the companion bill, HB 5120. It is dead for this year.

The insurance industry and business communities are working on a dual track to reverse **Washington** SB 5726, which enacted the lowest standard for insurance bad faith in the country. The coalition currently is seeking signatures to qualify for a referendum that would put the issue on the ballot for the voters to overturn in the November elections. In the meantime, the industry is working on a Governor's task force to see if corrective language can be worked out for the 2008 session. The Governor is a trial lawyer and was one of the lead attorneys on the tobacco litigation. She does, however, have the following concerns with the new law: 1) a clear bad faith standard is needed; 2) punitive damages are unlimited and 3) health insurers are exempt. Even if the Governor's task force can agree on meaningful corrective legislation, there is no guarantee

that it will pass in 2008. By mid-July, the industry will be able to gauge whether corrective legislation is realistic or whether the referendum is the only real avenue to further address this new law.

**--Defeated.** A business and industry coalition turned the tide in **Minnesota**, and bad faith legislation was defeated before the session adjourned. The House and Senate passed different bad faith bills, but the industry continued with an extraordinary lobbying and public relations effort; and neither bill passed before the session adjourned.

**New Hampshire** Senate Bill 188 is dead for the year. The Senate version of the bill would have subjected an insurer to the consumer protection law if a court of competent jurisdiction found that the insurer engaged in unfair claims settlement practices and would have allowed a third party to bring a direct action against an insurer for an unfair claims settlement practice, independent of any actions taken by the Commissioner. The House amended the bill by substituting provisions that would have increased the penalties for violation of the unfair claims practices law from \$2,500 to up to \$25,000 for each violation. The Senate did not concur with the House amendment, and the bill went to conference where it died when the conferees failed to reach an agreement by the June 19 deadline.

### **State Bond Thresholds**

**--Enactments.** **Florida** HB 985 increases the bond threshold for DOT projects from \$150,000 to \$250,000. **Georgia** HB 192 increases the threshold under which a letter of credit may be accepted in lieu of a bond. Instead of \$300,000, the new law provides that a letter of credit may be accepted on projects of less than \$750,000. **Texas** SB 657 increases the bond threshold from water districts from \$25,000 to \$50,000.

**--Bills on the Move.** **Connecticut** SB 1182 would increase the state bond threshold for payment bonds from \$50,000 to \$100,000. The bill is on the Governor's desk for signature. Last year, the threshold on performance was raised.

In **New York**, efforts are underway to amend the Wicks Act, which requires that separate contracts be competitively bid and awarded to a minimum of four general contractors for general construction, plumbing, electrical and heating and ventilation. Senate Bill 6146 recently was introduced in the New York Senate Rules Committee at the request of Governor Spitzer. The bill addresses payment and performance bonds by way of a new provision that would be added to the labor law. As drafted, SB 6146 would require every contract for a public work to contain a provision requiring payment and performance bonds. The bill neither states a bond amount nor a bond threshold. As drafted, the labor law would be amended to require payment and performance bonds from dollar one.

Section 137 of the state finance law, the Little Miller Act, would remain largely the same. The Little Miller Act currently requires a payment bond, but provides that it can be waived for contracts under \$100,000 and for contracts under \$200,000 if the contract is not subject to the multiple award requirements of the Wicks Act. SB 6146 would amend Section 137 to include a reference to performance bonds. When payment bonds are waived, retainage may be set at 20%.

The bill would amend the provision on waiver of payment bonds to include a reference to a waiver of performance or payment bonds.

Overall, SB 6146 is a pro-labor effort that goes beyond the Wicks Act to encourage use of union labor on public projects in New York. AB 9204 has been introduced as a companion bill in the Assembly. The Associated General Contractors and the AIA have reported that this is the agreed-upon bill that will pass in New York this year. There is little chance of any further amendments. The bill remained in the Senate Rules Committee when New York recessed for the summer.

**Rhode Island** HB 6335/SB 972 would increase the state bond threshold from \$50,000 to \$200,000. These bills were introduced late in the session and never moved. The legislature is adjourned, and the bills are dead. Before the 2008 session, however, SFAA will contact the bill sponsors to find out what is behind these bills. Because companion bills were introduced, it is likely that the issue will be back in 2008 unless it is addressed.

### **Individual Sureties**

The individual surety issue has arisen in **Pennsylvania** HB 445, which is a commercial surety bill that would require dog kennels to be licensed and bonded. The bond must be issued by a surety licensed in the state or “two sufficient individual sureties approved by the Secretary” (of Agriculture). SFAA believes that this is a bad precedent in permitting individual sureties, and in fact this conflicts with the Pennsylvania Insurance Code.

The Pennsylvania Insurance Code provides that insurance companies conduct the business of insurance in the Commonwealth, and private individuals, associations and partnerships are prohibited. The Code further requires bonds to be issued by a company duly licensed by the Insurance Department. Not only is it illegal under the Insurance Code for individuals to be sureties, it is also outside of the expertise of the Secretary of Agriculture to determine whether an individual is a “sufficient surety” and to permit such individuals to act as a surety company without a license in Pennsylvania. There is a lot of time to address this bill, and SFAA and AIA currently are working on a strategy to approach it.

### **Retainage**

**--Enactments.** **Tennessee** HB 1003 provides that retainage on public and private construction projects may not exceed 5%. The new law also requires that retainage be released within 90 days of completion or substantial completion, whichever occurs first. **Texas** HB 2074 provides that the DOT may retain up to 5% for the entire length of the project or may release it at any time before the project is completed.

**--Bills on the Move.** **California** SB 593 was amended to include some unusual retainage provisions. It would require the Department of Transportation (DOT) to withhold no retainage until 75% of the days allotted to the project have passed. At that point, the DOT can require retainage only if the percentage of working days elapsed exceeds the percentage of work completed by at least 15%. For example: If the contractor has 300 days to complete the job and has 30 days to go, the percentage of working days left is 10%. If the contractor has \$250,000 more work to do on a \$1 million job, the percentage of work to be completed is 25%. The public

owner could require retainage because the percentage of working days elapsed (90%) exceeds the percentage of work completed (75%) by 15%. Once the difference between these two amounts is less than 15%, any retainage held must be returned in the next progress payment.

SFAA thinks that this is too little, too late in terms of retainage. It also makes no sense to us to compare the percentage of working days, which is a value stated in numbers of days, to the percentage of work completed, which is a value stated in dollars. The system will be hard for the DOT to administer. It also may provide little protection for the State. According to the bill, once the percentages are under 15% any retainage must be returned to the general contractor, regardless of whether there are outstanding claims against the contractor for not paying subs and suppliers or whether there are change orders or other circumstances that warrant holding the retainage. SFAA worked with the Local Surety Associations to address this bill and the bill sponsor recently agreed to make this a two-year bill, meaning it won't be heard until 2008.

**New Jersey** AB 3649 would extend the 2005 retainage law for DOT projects to the construction and maintenance projects of the New Jersey Turnpike Authority. The bill would set retainage at 2% until substantial completion, after which 1% of a payment could be withheld. The Authority would be able to withhold 4% if the project is not progressing according to specifications. The bill is on its way to enactment.

**--Recent Introductions.** **Massachusetts** HB 3181 would require the escrow of retainage and allow the interest accrued to be paid to the contractor on public works projects.

**--Dead for 2007.** **Arizona** HB 2406 would have reduced retainage from 10% to 5% on a contracted commercial project. **Connecticut** HB 7202 would have reduced retainage on commercial construction contracts from an amount that does not exceed 7.5% to 5%. In all public projects, other than DOT projects, retainage would have been reduced from 10% to 5%. Under existing law, retainage on DOT projects is 2.5%.

### **Bonding on Mega Construction Projects**

**--Enactments.** **Florida** HB 985 increases the bond threshold for DOT projects from \$150,000 to \$250,000 and would permit the DOT to waive 100% bonds on contracts in excess of \$250 million. For such large projects, the DOT would be permitted to set the bond amount at some portion of the total contract price and accept other forms of security for amounts in excess of the bond.

**Florida** HB 1489 requires a 100% performance and payment bond for all other public projects, except for projects over \$250 million, for which the public owner can require the largest bond reasonably available, but not less than \$250 million. The existing statute was silent as to whether the bond had to be for 100% of the contract price.

### **Public Private Projects (PPPs)**

**--Enactments.** **Texas** SB 792 permits PPPs in specified toll way projects. The bill would require the private entity to provide payment and performance bonds or alternate security for the cost of constructing and maintaining the project. If the toll way authority finds it impracticable for the private entity to provide bonds or security in the amounts required, the authority will set

the amount of the bonds or alternative security. The bill would also provide that the authority may require alternative security in lieu or in addition to performance and payment bonds. Under the bill, the design and planning services, among other non-construction items, do not have to be bonded.

SFAA worked with the Texas Surety Federation, which was active in proposing amendments to assure a maximum amount of bonding on any PPPs authorized. The PPP concept had a lot of support, and the DOT wanted flexibility in the amount of security required. The major debate on the PPP bills centered around the terms and conditions of PPPs rather than surety bonding. The bills were hard to amend, and SB 792 was the result of compromise. The **Texas** Governor vetoed HB 447 and HB 1892, the latter of which started out as the companion bill to SB 792. The bonding provisions in the bills were similar to SB 792, but the bills were different in the terms and conditions under which PPPs could operate.

**--Bills on the Move. California** S 61 would authorize the DOT to enter into agreements with a private entity to construct a transportation project. Under the agreement, the DOT would be able to require performance and payment bonds, parent company guarantees, letters of credit or other acceptable forms of security. The bill would authorize the security to be in an amount equal to 100% or less of the value of the contract involved in the agreement. The amount of the security would be based on the DOT's determination of what would be required to adequately protect the public interest on a facility-by-facility basis. The bill has passed the Senate and is in the Assembly.

**--Carryover. Hawaii** HB 70 would authorize public private partnerships. The bill would permit the penal sum of the bond to be less than 100% of the value of the contract based on the DOT's determination. **Tennessee** HB 1205/SB 347 would authorize public private transportation projects and would require a comprehensive agreement with the private party, which would require bonds in forms and amounts satisfactory to the public entity.

**--Bill Status. Illinois** SB 378 would permit public private partnerships for transportation projects. The amount of the payment and performance bonds would be set forth in the public private agreement, or the transportation authority could determine the amount of the bonding necessary to protect the authority and the payment bond beneficiaries. The bill should be dead, but it has been parked in the Senate Rules Committee and the deadline for a floor vote on it has been extended continually. The current deadline now is December 31, 2007.

**--Dead. Arizona** SB 1635 would have permitted a public private project to construct highway "fast lanes". The private entity would have provided bonding as the DOT reasonably required. SFAA worked with AIA and the local surety association on amendatory language to clarify the bonding provisions, but the bill stalled and ultimately died. **Missouri** HB 595, which would have allowed public private partnerships for a period of 25 years and also would have permitted an annual bid bond, failed to pass. The bonding provisions in the bill would have required a payment bond required by Missouri law and a performance bond that covered the maximum amount of construction work the contractor performed in any year of the agreement.

### **Indemnity Agreements in Construction Contracts**

**--Dead. Arizona** HB 2607 would have extended the existing prohibition on indemnity agreements in private construction contracts to contracts for architect-engineer professional services.

### **Bond Guarantee Programs and Technical Assistance Programs**

**--Enactments. Florida** HB 1283/S 2860 create the Black Business Investment Board to assist in the development and expansion of black business enterprises, including a new program offering assistance in obtaining surety bonds and other credit instruments. The new Black Contractors Bond Trust Fund authorizes the Board to provide up to 90% bond guarantees.

**Oregon** HB 2776 extends the exemption for small and emerging contractors from one to five years from the requirement to file the new public works bond, which was enacted in 2005.

**Texas SB 704** amends the small contractor participation assistance program. The new law creates a technical assistance program for contractors to prepare bond application packages for public works projects in a format acceptable to bond underwriters and assist such contractors in obtaining bonds. Prior law provided that the program was applicable to contracts costing over \$20 million and had no such bonding assistance program. The new law now applies to public works projects that will involve a contract or aggregated multiple contracts with costs over \$1 million.

**--Bills on the Move. California** B 1491 would create the Small and Emerging Contractors Bonding Program pursuant to the Governor's Executive Order in 2006. This bill would require the Department of Transportation (DOT) to work in consultation with the Office of Small Business Advocate to establish a Small and Emerging Contractor Technical Assistance Program by September 1, 2008, to provide training and technical assistance to small contractors to improve their ability to obtain the surety bonds and liability insurance necessary to qualify for public works construction projects. The bill outlines the types of information that the training would have to provide as follows:

- Basic information on the purpose and use of surety bonds and liability insurance required in public works construction contracts in the State;
- Types of surety bonds and liability insurance policies required by public agencies awarding the contracts and typical minimum limits of coverage;
- Ways and means of purchasing surety bonds and liability insurance policies; the DOT would be able to distribute lists to program participants of insurance brokers, insurers and sureties that are licensed in the State and offer insurance services, liability insurance or surety bonds;
- A description of the minimum financial and experience criteria sureties and liability insurers use to evaluate the relative risk of contractors applying for surety bonds and liability insurance policies; information also would be provided on how those criteria are used to determine whether a contractor can qualify and for calculating the premiums;
- A description of state statutes and regulations applicable to contractors undertaking public works construction contracts, including, but not limited to, prevailing wage requirements, accounting practices, reporting requirements, jobsite health and safety requirements and injury and illness prevention programs. The information would have to

include a description of typical contractor practices used to comply with these statutory and regulatory requirements;

- Information on bidding procedures, differences in bidding as a prime contractor or subcontractor and the benefits and challenges of acting as a prime or subcontractor, as they relate to securing surety bonds and liability insurance;
- A description of public and private financial programs small contractors may utilize for the purpose of establishing sufficient capital necessary to obtain surety bonds and purchase liability insurance coverage; at a minimum, the program would have to provide information about loan and bond guarantees available through the California Small Business Expansion Fund under existing law.

The bill would require status reports on the program, including information on its impact and effectiveness. SFAA supports this program and will offer assistance in its development. The bill has passed the Assembly and is in the Senate.

**Illinois** SB 1511 still has life as the deadline for enactment has been extended until June 30. As amended and passed in the Senate, the bill would authorize the Capital Development Board to accept a “second party bond” if the contractor is a small business. A “second party bond” is one that “designates as principal, guarantor or both, a person or persons in addition to the person to whom the contract is proposed for award”. The bill is an attempt to add parties to a surety bond, probably with the intent of making bonds for small contractors more attractive for sureties to write. The original bill would have allowed the Board to waive bonds for small and minority-owned contractors. SFAA and AIA worked together to amend the bill in the House so that the Board could accept cash, letters of credit, U.S. debt obligations or debt obligations backed by the full faith and credit of the State of Illinois from small and minority businesses in lieu of surety bonds. The Senate still needs to concur with this amendment.

**--Bills on the Move.** There are two sets of companion bills in **New York** that would permit payment and performance bonds to be waived for small-, minority- and women-owned business on contracts under \$500,000: AB 3329/ SB 5199 and AB 8108/SB 2431. AB 3329 has passed the Assembly and is in the Senate, where the companion bill has never moved. SB 2431 was recently amended in the Senate Finance Committee to increase the threshold to \$1 million; but it is not moving, nor is AB 8108, its companion bill.

### **Prevailing Wages**

**California** AB 1076 amends the prevailing wage law, which already makes the surety liable for prevailing wages, along with the contractor and subcontractor. The bill would enhance enforcement by requiring payment for wages owed within 45 days after all administrative remedies and judicial review options has been exhausted. The bill has passed two committees in the Assembly and remains in the Appropriations Committee.

### **Electronic Bidding**

**Louisiana** SB 280 would permit electronic bidding by eliminating the requirement that all bid documents be submitted in writing. The bill also would require all bids on projects in excess of \$50,000 to be submitted with a bid bond. It would eliminate the options of a cashier’s check, certified check, money or company check. The bill is in conference committee.

### **Bidding Preferences**

**--Bills on the Move.** **Illinois** HB 634 would permit a 5% bid preference to bidders using biobased products. The bill is on the Governor's desk for signature. **New York** AB 8442 would require that a bidding preference be given to any state contractor, including construction, that provides its employees with employer-sponsored health coverage. The bill is on the Assembly floor.

**--Recent Introductions.** **New Jersey** AB 4276 would extend to public construction projects the preference to bidders that comply with retrofit requirements for off-road diesel equipment and on-road diesel vehicles.

### **Other**

**Illinois** HB 773 would enact a new prompt payment act. The bill would require owners to pay contractors within 15 days from the owner's approval of the application for payment. A payment application will be deemed approved if the owner has not provided a written reason for withholding the payment within 25 days. Contractors must pay subcontractors within 15 days of receipt of payment from the owner. The interest on late payments is 10%. The bill has passed both chambers in Illinois.